



MARTHA COAKLEY
ATTORNEY GENERAL

THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF THE ATTORNEY GENERAL
ONE ASHBURTON PLACE
BOSTON, MASSACHUSETTS 02108

(617) 727-2200
(617) 727-4765 TTY
www.mass.gov/ago

Testimony of Attorney General Martha Coakley
House Bill 3516, *An Act Regulating Compensation of Board Members of Public Charities*
Joint Committee on the Judiciary
September 27, 2011

Good afternoon Chairman O’Flaherty, Chairwoman Creem, and members of the Joint Committee. Thank you for the opportunity to testify today in support of House Bill 3516, *An Act Regulating Compensation of Board Members of Public Charities*. This legislation, which I have co-sponsored with Senator Mark Montigny and House Ways and Means Vice-Chair Martha Walz, provides that unless they obtain approval from the Office of the Attorney General’s Public Charities Division (“AGO”), public charities registered in Massachusetts need to have voluntary board directors.

Our Office’s Public Charities Division oversees the Commonwealth’s 25,000 nonprofit charitable organizations that range in size and complexity from our largest universities and health care systems to small, neighborhood-based social service organizations and youth sport leagues.

As part of our statutory mandate to oversee public charities and the application of charitable funds, we spent the last two years investigating the practice of board member compensation at Massachusetts’ four major charitable health insurers: Blue Cross Blue Shield, Fallon Community Health Plan, Harvard Pilgrim Health Care and Tufts Health Plan. We began that investigation with the understanding that the vast majority of public charity directors

volunteer their time, and for good reason. Indeed, the Supreme Judicial Court has recognized voluntary board service as a primary indicator that an organization's purposes are charitable and nationally recognized governance standards for charities establish that board members are generally expected to serve without compensation. The practice of board members voting to compensate themselves is more than contrary to the norms applied to such volunteer service. It involves an unavoidable conflict between board members' personal financial interests and their obligation to safeguard the organization's charitable resources. Moreover, the practice is currently not subject to any external review or direct oversight.

The four health insurance organizations enjoy significant tax and other benefits due to their charitable status, and we gave them extensive opportunities to justify why they should be treated differently from the overwhelming majority of other charitable boards.

They offered similar explanations for why their charities are unique, including that they were more complex, that their directors committed significant time and effort, and that they must pay their directors to compete for talent nationwide.

We found their arguments to be unsupported and unpersuasive. Their organizations are no more complex than many large hospitals and universities. There was no evidence provided that their directors worked harder than the boards of other large sophisticated public charities. And the argument that they must compete for nationwide talent fell flat when we discovered nearly all of their directors reside right here in Massachusetts.

We issued a report, which is attached hereto, outlining our full findings in April. Following that report, two of the plans – Blue Cross and Fallon – rightfully suspended the practice. The other two – Harvard Pilgrim and Tufts Health Plan - affirmatively decided to continue compensating their directors.

As a result of this investigation, our Office took two actions. First, to bring further

transparency to the issue of director compensation, the AG's Office will require annual statements from all Massachusetts based public charities that compensate independent directors explaining, in detail, the basis and rationale for the practice. Those statements, director compensation levels, and AGO evaluations will form the basis of an annual public report on director compensation practices at public charities.

The second action was the filing of this legislation before you today which is aimed at prohibiting these organizations from continuing to compensate directors without approval from the Attorney General's Office. Specifically, the proposed legislation would (1) prohibit Massachusetts-based public charities from compensating their directors unless they obtain approval from the Chief of the Attorney General's Public Charities Division; and (2) provide the AGO with the authority to rescind any such approval upon a finding that the amount of compensation paid is more than reasonably necessary.

Even though the practice of compensating independent directors for service on a charitable board is extraordinarily rare, we did not propose an outright ban of the practice. We recognize that some organizations may be able to justify the practice and we intend to issue regulations or guidance to address appropriate justifications for compensating directors and to provide certainty regarding the difference between compensation and reimbursement of expenses, or other non-income. We do believe, however, that unjustifiable compensation of charitable board directors creates inherent conflicts of interest that are currently not adequately disclosed or reviewed. Providing the tools set forth in this bill is the most effective way to protect the public interest and ensure the proper use of charitable funds.

As such, I urge the committee to report this bill out favorably. Thank you.